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CASE NOTES

LOADING SOFTWARE INTO RAM CREATES A "COPY"

MAI Systems Corp. v. Peak Computer Inc., 991 F.2d 511, 26

U.S.P.Q.2d (BNA) 1458, (9th Cir. 1993), *cert. dismissed*, 114 S. Ct. 671, 62 U.S.L.W. 3473, 1994 U.S. Lexis 937 (1994).

Brian J. Murphy†

I. INTRODUCTION

On April 9, 1993, the Court of Appeals for the Ninth Circuit in *MAI Systems Corp. v. Peak Computer Inc.*¹ notably held that loading software into a computer's random access memory ("RAM") creates a copy under section 101 of the Copyright Act.² Although the court acknowledged that it had no "specific" authority for this proposition and that those authorities cited were "somewhat troubling," the court took its conclusion to be "generally accepted."³

MAI Systems Corporation (MAI) previously manufactured computers and designed accompanying software, and remains in business providing supplies and service, including maintenance and training, for thousands of active users of their machines.⁴ It is estimated that the global market for such service and maintenance "produces revenues in excess of \$50 million dollars per year."⁵ MAI's customer service business is critical to its survival, providing both profits and the capital necessary to maintain a field staff and updated software.⁶

MAI's copyrighted software includes both diagnostic and operating system software—each containing MAI trade secrets. Their computer systems are considered unique in the business because MAI

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1. 991 F.2d 511 (9th Cir. 1993), *cert. dismissed*, 114 S. Ct. 671 (1994) [hereinafter MAI Systems II].

2. 17 U.S.C. § 101 (1988).

3. *MAI Systems II*, 991 F.2d at 519.

4. *MAI Systems Corp. v. Peak Computer, Inc.*, No. CV 92-1654-R, 1992 U.S. Dist. LEXIS 21829 at *3 (D. Cal. Mar. 30, 1992) [hereinafter MAI Systems I].

5. *Advanced Computer Services of Michigan, Inc. v. MAI Systems Corp.*, 161 B.R. 771, 1993 U.S. Dist. LEXIS 17985 at *2 (E.D. Va. Dec. 13, 1993).

6. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829, at *7.

"parts and operating system software do not work in other manufacturers' minicomputers."⁷ Significantly, MAI's practice is to license, rather than sell, this software to its customers.⁸ The software licensing agreements expressly restrict access to the software to the customers' employees, MAI representatives or others authorized by MAI; and also contemplate termination of the agreement for unauthorized access.⁹ By the terms of the agreements, such unauthorized use subjects both the customer and the third party to copyright infringement liability.¹⁰ This conclusion comports with section 117 of the Copyright Act, which accords copyright protection exclusively to "owners," and not to mere licensees like MAI's customers.¹¹

Peak Computer Inc. (Peak) provides routine maintenance and emergency repairs on computers in the southern California area.¹² Over one hundred of Peak's clients, accounting for fifty to seventy percent of their business, require service on MAI computers.¹³ Special training or skill in the maintenance and service of MAI computers and an inventory of MAI parts are typically required for a company to service customers with the unique MAI systems.¹⁴ In the course of this maintenance, Peak must operate their customers' MAI computers and MAI software.¹⁵

In 1991, several MAI employees, including customer service manager Eric Francis, left their positions to work for Peak, and a number of MAI customers switched to Peak upon learning of the move.¹⁶ Francis, in particular, entered into several agreements during his employment with MAI in which he agreed to keep MAI trade secrets and proprietary information confidential, to refrain from soliciting MAI's employees, and to neither solicit MAI customers nor provide services competitive with MAI within one year after his termination from MAI.¹⁷

7. *Advanced Computer Services*, 1993 U.S. Dist. LEXIS 17985 at *3.

8. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *4.

9. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *4 n.2. The licenses also provide that any attempt of the customer to license or sublicense or otherwise transfer the software to others immediately terminates its license. Accordingly, when a customer attempts to have a third party maintenance organization such as Peak service the software without first obtaining the permission of MAI, the license terminates, leaving both the customer and any third party user of the system other than the copyright owner in the position of being infringers. *Id.*

10. *Id.*

11. 17 U.S.C. § 117 (1988).

12. *MAI Systems II*, 991 F.2d at 513.

13. *Id.*

14. *Advanced Computer Services*, 1993 U.S. Dist. LEXIS 17985 at *3.

15. *MAI Systems II*, 991 F.2d at 513.

16. *Id.*

17. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *9.

In 1992, MAI filed suit against Peak, its president, and Francis alleging copyright infringement, trade secret misappropriation, false advertising and unfair competition stemming from Peak's maintenance activities and Francis's move.¹⁸ This appeal concerns consolidated issues arising from preliminary and permanent injunctions granted and stayed during the district and appellate court processes.¹⁹

II. COPYRIGHT INFRINGEMENT

The district court issued a permanent injunction against Peak for alleged copyright infringement stemming from "(1) Peak's running of MAI software licenced [sic] to Peak customers; (2) Peak's use of unlicensed software at its headquarters; and, (3) Peak's loaning of MAI computers and software to it customers."²⁰ The Ninth Circuit reviewed each claim independently.

A. Peak's Running of MAI Software Licensed to Peak's Customers

As to the first, and most important, claim for copyright infringement, the Court of Appeals acknowledged that a plaintiff must prove both ownership of a copyright and a "copying of protectable expression" beyond the scope of a license."²¹ MAI's copyright was undisputed, and the court held that any copying done by Peak was outside the scope of MAI customers' software licenses that, as noted above, expressly prohibit unauthorized third party access.²²

Section 101 of the 1976 Copyright Act defines "copies" as "material objects . . . in which a work is *fixed* by any method now known or later developed, and from which the work can be perceived, reproduced, otherwise communicated, either directly or with the aid of a device."²³ A work is statutorily "fixed in a tangible medium of ex-

18. *Id.* at *29.

19. The district court granted a preliminary injunction against Peak, prohibiting them variously from infringing MAI copyrights, misappropriating MAI trade secrets, soliciting MAI customers, and maintaining MAI computers. In turn, the Ninth Circuit stayed the preliminary injunction insofar as it prohibited Peak from maintaining MAI computers, but refused to stay the district court proceedings. The district court subsequently granted a partial summary judgment and entered a permanent injunction on the copyright infringement and trade secret misappropriation causes of action. The Ninth Circuit then stayed the permanent injunction, and consolidated appeals of both the preliminary injunction and portions of the permanent injunction relating to trademark infringement and false advertising—the latter consolidated appeals are reviewed in the instant action. *MAI Systems II*, 991 F.2d at 513-16.

20. *MAI Systems II*, 991 F.2d at 517.

21. *Id.* (quoting *S.O.S., Inc. v. Payday, Inc.*, 886 F.2d 1081, 1085 (9th Cir. 1989)).

22. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *4.

23. 17 U.S.C. § 101 (emphasis added).

pression when its embodiment in a copy[,] . . . by or under the authority of the author, is sufficiently permanent or stable to permit it to be perceived, reproduced or otherwise communicated.”²⁴ Although Peak first attempted to argue that MAI software was not used in the process of Peak’s maintenance, the district court observed that Francis admitted that the operating system was necessary in this process and that the diagnostic software was used by Peak.²⁵ The Ninth Circuit found that Peak needed to “turn on” their customers’ MAI computers, which in turn loaded the operating system into the computer’s RAM, to determine whether the system was functional and to view the system’s error log.²⁶ The error log, which is part of the operating system, chronicles the activities of the computer and thus is a useful resource in diagnosing the system’s defects.

Peak vigorously insisted that loading of the copyrighted software into RAM does not create a copy that is fixed. However, the court found “no specific facts” which demonstrate that the copy created in the RAM is *not* fixed.²⁷ Although it located “no case specifically hold[ing] that the copying of software into RAM creates a ‘copy’ under the Copyright Act,” the court held that it is “generally accepted” that loading software into RAM creates a copy under the Copyright Act.²⁸ The court cited as its authority *Vault Corp. v. Quaid Software Ltd.*,²⁹ *Nimmer on Copyright*³⁰ and the CONTU report,³¹ but distinctly acknowledged that these sources “do not specify that a copy is created regardless of whether the software is loaded into the RAM, the hard disk or the read only memory (‘ROM’).”³² Nonetheless, the court held that, because the copy created in RAM can be “perceived, reproduced or otherwise communicated,” the loading of software into RAM creates a “copy” under section 101 of the Copyright Act.³³

24. *Id.*

25. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *22 n.6.

26. *MAI Systems II*, 991 F.2d at 518.

27. *Id.*

28. *Id.* at 519.

29. 847 F.2d 255 (5th Cir. 1988) (“the act of loading a program from a medium of storage into a computer’s memory creates a copy of the program”).

30. “Inputting a computer program entails the preparation of a copy.” 2 NIMMER, NIMMER ON COPYRIGHT § 8.08 at 8-105 (1983).

31. “[T]he placement of a work into a computer is the preparation of a copy.” FINAL REPORT OF THE NATIONAL COMMISSION ON THE NEW TECHNOLOGICAL USES OF COPYRIGHTED WORKS, H.R. REP. NO. 1307, 96th Cong., 2d Sess., pt. 1, at 13 (1978).

32. *MAI Systems II*, 991 F.2d at 519.

33. *Id.*

B. Peak's Use of Unlicensed Software at its Headquarters

The district court, in its findings of fact, noted that Peak has "half a dozen" operating MAI computers," although it had only acquired a license to operate one of them.³⁴ The district court granted, and the Ninth Circuit affirmed, a summary judgment in favor of MAI for copyright infringement for Peak's unauthorized use; and the Ninth Circuit likewise affirmed the lower court's issuance of a permanent injunction on this issue.³⁵

C. Peak's Loaning of MAI Computers and Software to its Customers

MAI asserted numerous causes of action for copyright infringement derived from allegedly misleading, inaccurate and infringing information contained in various Peak advertising brochures.³⁶ MAI contends that Peak illegally loaned out MAI computers to its customers in accordance with their advertisements, which described the availability of loaner computers.³⁷ Although Peak's president admitted that MAI computers were among those available for loan, it was never proven that MAI computers were ever actually loaned out.³⁸ Nevertheless, the appeals court affirmed the permanent injunction issued by the district court because there was a real threat of future violations.³⁹

III. MISAPPROPRIATION OF TRADE SECRETS

MAI also asserted a cause of action for misappropriation of its trade secrets in connection with "(1) MAI customer database; (2) MAI Field Information Bulletins ('FIBs'); and, (3) MAI software."⁴⁰ The lower court granted a summary judgment in favor of MAI and issued an injunction on all of the trade secret claims.⁴¹ The Ninth Circuit reviewed the merits of each claim separately.

The Ninth Circuit concluded that MAI's customer database was protectable as a trade secret,⁴² as defined in the Uniform Trade Secret Act which has been adopted in California.⁴³ The court opined that the

34. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *19-20 (quoting deposition testimony of Vincent Chiechi, named defendant and president of Peak).

35. *MAI Systems II*, 991 F.2d at 519.

36. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *20.

37. *Id.*

38. *Id.* at *21.

39. *MAI Systems II*, 991 F.2d at 520.

40. *Id.*

41. *MAI Systems I*, 1992 U.S. Dist. LEXIS 21829 at *52.

42. *MAI Systems II*, 991 F.2d at 520.

43. CAL. CIV. CODE §§ 3426-3426.11 (West Supp. 1994).

database has the requisite "potential economic value" because it permits a competitor to identify and target customers already using MAI systems.⁴⁴ The court also found that MAI took the necessary steps to conceal this information.⁴⁵ The database was held to be misappropriated, even though former MAI manager Francis may not have physically taken any portion of the list to Peak, because Francis improperly solicited MAI customers by paying them personal visits in an attempt to persuade them to switch over to Peak.⁴⁶

Although the Ninth Circuit found that the FIBs were protectable as trade secrets, it recognized a genuine issue of material fact as to whether Peak ever used any of the FIBs.⁴⁷ As a consequence, the appeals court reversed the district court's summary judgment on this particular claim and vacated that portion of the permanent injunction.⁴⁸ Likewise, the appeals court held that, while computer software can qualify as a trade secret, MAI never specifically identified the trade secrets existing in the software.⁴⁹ The appeals court similarly reversed the summary judgment and vacated the permanent injunction to the extent to which they addressed the issue of trade secret misappropriation of the software.⁵⁰

IV. BREACH OF CONTRACT AND PRELIMINARY INJUNCTION

The Ninth Circuit also affirmed the lower court's grant of summary judgment for Francis's breach of his contractual obligations to MAI.⁵¹ Furthermore, the district court granted a preliminary injunction against Peak for trademark infringement in response to Peak's advertisements.⁵² These ads implied that Peak was a licensed MAI dealer and that Peak's activities were approved by MAI.⁵³ Peak contended in its appeal that the lower court erred in granting the preliminary injunction because it neglected to consider the factors enunciated in relevant case law in its decision that a "likelihood of confusion" existed.⁵⁴ The Ninth Circuit decided that the lower court did not

44. *MAI Systems II*, 991 F.2d at 521.

45. *Id.*

46. *Id.* at 521-22.

47. *Id.* at 522.

48. *Id.*

49. *MAI Systems II*, 991 F.2d at 522 (to sustain a trade secret misappropriation cause of action, a plaintiff "must identify the trade secrets and carry the burden of showing that they exist").

50. *Id.* at 522-23.

51. *Id.* at 523.

52. *Id.*

53. *Id.*

54. *MAI Systems II*, 991 F.2d at 523.

abuse its discretion by failing to analyze each particular factor because a preliminary injunction determination is necessarily not a full hearing.⁵⁵ Finally, the Ninth Circuit ruled that the district court's grant of a preliminary injunction in MAI's favor for false advertising was supported by the record and that the lower court did not abuse its discretion.⁵⁶

VI. EPILOGUE

Not surprisingly, this Ninth Circuit decision has spawned more litigation. In April 1993, MAI filed a petition for bankruptcy and reorganization under Chapter 11 in Delaware Bankruptcy Court.⁵⁷ Some time also in April 1993, MAI allegedly sent out numerous "cease and desist" letters to a group of companies who, like Peak, compete with MAI for the business of servicing customers with MAI systems.⁵⁸ Specifically, these letters mentioned MAI's victory in the Ninth Circuit and demanded that the companies cease and desist from "any activity involving copying of MAI's operating system software, including 'loading' or 'booting' the software."⁵⁹

In subsequent months, these companies filed a copyright and anti-trust action against MAI in the United States District Court for the Eastern District of Virginia.⁶⁰ Plaintiffs in the Virginia district court action allege that MAI is engaged in "a plan to restrict competition in the market for . . . [such] maintenance . . . by refusing to authorize plaintiffs and other service organizations to load and use the MAI operating system software in connection with servicing or repairing MAI computers."⁶¹ In particular, plaintiffs contend that MAI is tying the sale of its copyrighted operating system software to the sale and maintenance services in contravention of sections 1 and 2 of the Sherman Act.⁶² The Delaware bankruptcy court annulled the automatic stay of proceedings which otherwise would have precluded this action, and the Virginia district court is now proceeding on the merits of these

55. *Id.*

56. *Id.*

57. See *Advanced Computer Services*, 1993 U.S. Dist. LEXIS 17985 at *2.

58. *Id.* at *5.

59. *Id.*

60. *Id.* at *2.

61. *Id.* at *4, *5.

62. *Advanced Computer Services*, 1993 U.S. Dist. LEXIS 17985 at *2-*3, *6. A number of recent decisions have addressed this issue of tying in the intellectual property arena. See *Service & Training, Inc. v. Data General Corp.*, 963 F.2d 680 (4th Cir. 1992); *Virtual Maintenance, Inc. v. Prime Computer, Inc.*, 957 F.2d 1318 (6th Cir.) *vacated and remanded*, 113 S. Ct. 314 (1992); *Image Technical Servs., Inc. v. Eastman Kodak Co.*, 903 F.2d 612 (9th Cir. 1990), *aff'd* 112 S. Ct. 2072 (1992).

causes of action against MAI.⁶³ Relying in part on the Ninth Circuit's decision, the Virginia district court held that MAI had established direct infringement by the plaintiffs' loading of MAI software into RAM.⁶⁴ Interestingly, the district court also sustained MAI's motion for summary judgment on the tying claim, primarily because plaintiffs could not demonstrate that "the licensing of MAI software was expressly or implicitly conditioned upon the purchase of MAI computer equipment servicing"—a necessary element of a tying claim.⁶⁵

In review, these disputes have all arisen due to MAI's practice of licensing, rather than selling, its software to its customers. When independent service organizations attempted to service MAI machines they inevitably loaded MAI software, creating a copy of the copyrighted software, and subjecting them to infringement liability. This decision comports with public policy whereby MAI should be allowed to license its software to whomever it chooses. This is true even if this policy dissuades buyers of MAI systems because their maintenance choices are limited since, in effect, MAI is only restricting its own potential market.

63. *Advanced Computer Services*, 1993 U.S. Dist. LEXIS 17985 at *15.

64. *Id.* at *14-*23.

65. *Id.* at *41.